

**Updated Informative Digest for the State Board of Equalization's
Adoption of Proposed Amendments to California Code of Regulations,
Title 18, Section 1598.1, *Diesel Fuel Prepayment Exemption***

The State Board of Equalization (Board) held a public hearing regarding the proposed amendments to California Code of Regulations, title 18, section (Regulation) 1598.1, *Diesel Fuel Prepayment Exemption*, on February, 24, 2015. During the public hearing, the Board unanimously voted to adopt the proposed amendments to Regulation 1598.1 without making any changes.

The Board did not receive any written comments regarding the proposed regulatory action and no interested parties appeared at the public hearing on February 24, 2015, to comment on the proposed regulatory action. There have not been any changes to the applicable laws or the effect of, the objective of, and anticipated benefits from the adoption of the proposed amendments to Regulation 1598.1 described in the informative digest included in the notice of proposed regulatory action. The informative digest included in the notice of proposed regulatory action provides:

Summary of Existing Laws and Regulations

California imposes sales tax on retailers for the privilege of selling tangible personal property at retail. (RTC, § 6051.) Unless an exemption or exclusion applies, the tax is measured by a retailer's gross receipts from the retail sale of tangible personal property in California. (RTC, §§ 6012, 6051.) Although sales tax is imposed on retailers, retailers may collect sales tax reimbursement from their customers if their contracts of sale so provide. (Civ. Code, § 1656.1; Cal. Code Regs., tit. 18, § 1700, subd. (a)(1).)

RTC section 6480.1 provides, in part, that at any time the diesel fuel tax is imposed or would be imposed on any removal, entry, or sale in this state of diesel fuel, the supplier shall collect prepayment of retail sales tax from the person to whom the diesel fuel is sold. For purposes of the imposition of the prepayment of sales tax on diesel fuel, RTC section 6480, subdivision (c), provides that the term "diesel fuel" is defined pursuant to the Diesel Fuel Tax Law (commencing with RTC section 60001). In addition, RTC section 6480.9 provides an exemption from the sales tax prepayment requirement on certain sales of diesel fuel for agricultural purposes, and requires a person purchasing diesel fuel that is exempt from the sales tax prepayment requirements to issue an exemption certificate to the seller in accordance with any instructions or regulations prescribed by the Board.

The Board adopted Regulation 1598.1 in 2003. Regulation 1598.1 specifies the conditions under which the exemption provided in RTC

section 6480.9 applies to the prepayment of sales tax on diesel fuel. Regulation 1598.1 also prescribes the exemption certificate required by RTC section 6480.9 and the appendix to Regulation 1598.1 contains an exemption certificate form, which may be used to claim the diesel fuel prepayment exemption.

In 2003, RTC section 60022, subdivision (c), expressly provided that “‘Diesel fuel’ does not include the water in a diesel fuel and water emulsion of two immiscible liquids of diesel fuel and water, which emulsion contains an additive that causes the water droplets to remain suspended within the diesel fuel, provided the diesel fuel emulsion meets standards set by the California Air Resources Board.” Subdivision (a)(4) of Regulation 1598.1 refers to RTC section 6480, subdivision (c) and RTC section 60022, and incorporates the definition of diesel fuel from RTC section 60022 (2003), including the provisions of section 60022, subdivision (c). However, on January 1, 2007, RTC section 60022 (2003) was repealed and replaced by new section 60022, and new section 60022 does not contain the provisions that were formerly in subdivision (c) of section 60022 (2003).

Furthermore, subdivision (b) of Regulation 1598.1 lists a number of requirements that must be satisfied in order for the exemption provided in RTC section 6480.9 to apply to the prepayment of sales tax on diesel fuel sold to a retailer. As relevant here, subdivision (b)(4) of the regulation requires that “[d]uring the calendar year immediately preceding any purchases of diesel fuel, [the retailer] sold diesel fuel to diesel fuel consumers in which the gross receipts from such sales exceeded 25 percent of that retailer’s total taxable sales.” The last paragraph of subdivision (b) provides guidance about how to calculate the percentage referred to in subdivision (b)(4), and the guidance refers to amounts entered on specific lines of sales and use tax returns. However, when a taxpayer files its return via the Board’s online services, specific line numbers are not included.

Effect, Objective, and Benefits of the Proposed Amendments to Regulation 1598.1

As a result of the January 1, 2007, repeal of the provisions formerly in RTC section 60022, subdivision (c), the definition of diesel fuel in Regulation 1598.1 is no longer consistent with the current provisions of RTC section 60022. Therefore, Board staff determined that it was necessary to amend Regulation 1598.1 so its definition of diesel fuel is based upon the current definition of the term diesel fuel contained in section 60022 of the Diesel Fuel Tax Law, as provided in RTC section 6480, subdivision (c).

Interested Parties Process

The Board's Business Taxes Committee (BTC) staff prepared draft amendments deleting the third paragraph from the definition of diesel fuel in subdivision (a)(4) of Regulation 1598.1. BTC staff subsequently prepared a discussion paper, and provided the discussion paper and its draft amendments to Regulation 1598.1 to the interested parties. On July 15, 2014, BTC staff conducted an interested parties meeting to discuss the draft amendments.

Since BTC staff did not receive any inquiries or written comments regarding its draft amendments during or subsequent to the July 15, 2014, interested parties meeting and staff had no changes to its recommendation to amend Regulation 1598.1, BTC staff did not prepare a second discussion paper and cancelled the second interested parties meeting that was previously scheduled to discuss staff's draft amendments. Staff also notified interested parties that comments could be submitted up to September 25, 2014, for consideration in the preparation of the Formal Issue Paper regarding the draft amendments. However, staff did not receive any other comments.

November 19, 2014 BTC Meeting

Subsequently, staff prepared Formal Issue Paper 14-009 and distributed it to the Board Members for consideration at the Board's November 19, 2014, BTC meeting. Formal Issue Paper 14-009 recommended that the Board approved and authorize publication of the amendments to Regulation 1598.1 (discussed above) to delete the third paragraph in Regulation 1598.1, subdivision (a)(4), so the regulation's definition of diesel fuel is consistent with the operative provisions of RTC section 60022. Formal Issue Paper 14-009 recommended that the Board revise the last paragraph in Regulation 1598.1, subdivision (b), so that it provides the same general guidance about how to calculate the percentage referred to in subdivision (b)(4) of the regulation, but without referring to amounts entered on specific lines of sales and use tax returns. Formal Issue Paper 14-009 also recommended that the Board replace the capital "A" with a lower case "a" at the beginning of the word "Article" in the appendix to Regulation 1598.1 to make the word consistent with the reference to "article" in subdivision (d)(1) of the regulation and consistent with the citation format prescribed in the California Style Manual.

During the November 19, 2014, meeting, the Board Members unanimously voted to propose the amendments to Regulation 1598.1 recommended in the formal issue paper. The Board determined that the proposed amendments to Regulation 1598.1 are necessary to have the

effect and accomplish the objective of ensuring that the definition of diesel fuel in the regulation is consistent with the current definition of diesel fuel in the Diesel Fuel Tax Law, and ensuring that the regulation provides clear guidance to all taxpayers, including taxpayers who file returns via the Board's online services, about how to calculate the percentage referred to in subdivision (b)(4) of the regulation.

The Board also anticipates that the proposed amendments to Regulation 1598.1 will reduce confusion, promote fairness, and benefit sellers, retailers, Board staff, and the Board by providing a definition for the term diesel fuel that is consistent with the applicable statutory definition, and providing clear guidance about how to calculate the percentage referred to in subdivision (b)(4) of the regulation.

The Board has performed an evaluation of whether the proposed amendments to Regulation 1598.1 are inconsistent or incompatible with existing state regulations and determined that the proposed amendments are not inconsistent or incompatible with existing state regulations because Regulation 1598.1 is the only state regulation providing an exemption from the prepayment of sales tax on diesel fuel. The Board is aware that California Code of Regulations, title 18, section (Regulation) 1533.2, *Diesel Fuel Used in Farming Activities and Food Processing*, also defines the term "diesel fuel" and the Board is separately proposing to amend the definition for the term diesel fuel in Regulation 1533.2 so that it consistent with the current definition of the term diesel fuel in RTC section 60022 and the proposed amendments to the definition of the term diesel fuel in Regulation 1598.1. In addition, the Board has determined that there are no comparable federal regulations or statutes to Regulation 1598.1 or the proposed amendments to Regulation 1598.1.